



**REPORT OF THE AUDITOR OF PUBLIC ACCOUNTS
AUDIT OF THE PERSONNEL CABINET'S
PAYROLL AND PERSONNEL FUNCTIONS**

**Made as Part of the Statewide Single Audit
of the Commonwealth of Kentucky**

For the Year Ended June 30, 2001

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EXECUTIVE SUMMARY

Report of the Auditor of Public Accounts Audit of the Personnel Cabinet's Payroll and Personnel Functions For the Year Ended June 30, 2001

BACKGROUND: The Single Audit Act of 1984, subsequent amendments, and corresponding regulations, require the auditing of financial statements and the compliance and internal controls applicable to federal moneys received by the Commonwealth. To comply with these requirements, we audited internal controls and compliance at both the central and agency level. This summary is on our audit of one (1) organizational unit of the Commonwealth, the Personnel Cabinet's payroll and personnel functions.

Among other broad responsibilities, the Personnel Cabinet is responsible for the following:

- Providing executive policy and management support to the departments/divisions of the Cabinet and the Commonwealth;
- Promulgating administrative regulations;
- Conducting investigations on all matters relating to the personnel laws and rules;
- Maintenance of central personnel files;
- Processing personnel documents and position actions; operating and maintaining a uniform payroll system;
- Certifying payrolls;
- Monitoring and assisting state agencies in complying with the provisions of the Federal Fair Labor Standards Act;
- Preparing and maintaining job classification and compensation plans for state employees, including the review of all personnel position actions, job audits, revision of class specifications, and salary surveys; and
- Coordinating and implementing employment performance evaluation systems through state government.

The Commonwealth employed 43,643 people for the fiscal year ended June 30, 2001 at a cost of \$1,802,231,131.80. These figures represent an increase of 1.59% and .05%, respectively.

SUMMARY OF AUDITOR'S RESULTS:

Financial Statement Accounts

Reportable Condition:

We noted one reportable condition for FY 2001. Problems noted in past audits continue to exist. Procedures relating to logical access security continue to be a problem, with exceptions being noted in the Application Access System and Customer Information Control System, as well as personnel libraries, production data, and security files.

Other Matters:

Our audit noted no new Other Matter findings for FY 2001. We noted past problems with internal controls over redeposit of checks at the Administrative Office of the Courts (AOC) had been resolved. However, we noted continuing problems with AOC concerning internal controls over timesheets during FY 2001. The AOC has implemented an automated timesheet in the Frankfort office effective July 1, 2002. The automated time sheet program will be fully operational January 2003 when it is implemented for the employees in Circuit Court Clerks' offices throughout the state. We believe this will resolve any continuing problems related to this finding.

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INTRODUCTION

**PERSONNEL CABINET
INTRODUCTION
FOR THE YEAR ENDED JUNE 30, 2001**

Introduction

The Auditor of Public Accounts (APA), acting as principal auditor in conjunction with various certified public accounting firms, annually performs a statewide single audit of the Commonwealth of Kentucky. This audit allows the Commonwealth to comply with federal audit requirements as set forth in the Single Audit Act of 1984, as amended by Public Law 104-156, and the regulations contained in the Office of Management and Budget (OMB) Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

Schedule of Expenditures of Federal Awards

The Personnel Cabinet did not receive federal monies; therefore, a Schedule of Expenditures of Federal Awards is not required.

Schedule of Findings and Questioned Costs

The Schedule of Findings and Questioned Costs consists of three (3) sections:

- Summary of Auditor's Results,
- Financial Statement Findings, and
- Federal Award Findings and Questioned Costs.

The audit finding number and classification (as reportable, material, or other matter) are provided as part of the audit opinion summary. Major programs audited are listed on the summary of auditor's results. The financial statement findings list the audit findings related to the financial statements (required to be reported in accordance with *Government Auditing Standards*). The federal award findings and questioned costs lists all findings related to federal awards. Generally, the state agency, CFDA number and program, federal agency, pass-through agency, and the compliance area to which the finding relates are presented. In both reports, reportable conditions and reportable instances of noncompliance are presented first, then material weaknesses and material instances of noncompliance, then other matters.

Summary Schedule of Prior Audit Findings

Audit findings reported in the Schedule of Findings and Questioned Costs for the fiscal year ended June 30, 2000, as well as any previous findings which have not been resolved, are reported in the Summary Schedule of Prior Audit Findings for the fiscal year ended June 30, 2001. If the APA determines the agency's Summary Schedule of Prior Audit Findings materially misrepresents the status of any prior audit finding, a new audit finding is issued and reported in the Schedule of Findings and Questioned Costs.

**PERSONNEL CABINET
INTRODUCTION
FOR THE YEAR ENDED JUNE 30, 2001
(CONTINUED)**

Summary Schedule of Prior Audit Findings (Continued)

The Summary Schedule of Prior Audit Findings is organized based on whether the prior year finding was reportable, material, or other matter. The findings of each classification are categorized as (1) fully corrected, (2) not corrected or partially corrected, (3) corrective action taken differs significantly from corrective action previously reported, or (4) finding no longer valid or does not warrant further action.

Audit Approach

Our audit was conducted in accordance with the Single Audit Act Amendments of 1996, OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, *Government Auditing Standards* (also referred to as the Yellow Book), and auditing standards generally accepted in the United States of America. The scope of the statewide single audit for the year ended June 30, 2001 included:

- An audit of the general-purpose financial statements and required supplementary schedules in accordance with auditing standards generally accepted in the United States of America; and
- An audit of the internal control applicable to the Personnel Cabinet to the extent necessary to consider and test the internal accounting and administrative control systems as required.

The APA conducted the audit of internal controls, focusing on the following objectives:

- Considering the internal control in order to determine auditing procedures on the general-purpose financial statements of the Commonwealth.

**PERSONNEL CABINET
INTRODUCTION
FOR THE YEAR ENDED JUNE 30, 2001
(CONTINUED)**

List of Abbreviations/Acronyms Used in This Report

AOC	Administrative Office of the Courts
APA	Auditor of Public Accounts
CFDA	Catalog of Federal Domestic Assistance
CICS	Customer Information Control System
COBOL	Common Business Oriented Language
Commonwealth	Commonwealth of Kentucky
FY	Fiscal Year
GOT	Governor's Office of Technology
ID	User Identification (associated with computer usage)
JCL	Job Control Language
KRS	Kentucky Revised Statutes
MARS	Management Administrative and Reporting System
NA	Not applicable
OMB	Office of Management and Budget
PERS	Personnel Cabinet
Personnel	Personnel Cabinet
Security Policy	Computer Security Policy/Procedures Manual
UPPS	Uniform Payroll and Personnel System
U.S.	United States

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REPORT ON COMPLIANCE AND ON INTERNAL CONTROL



EDWARD B. HATCHETT, JR.
AUDITOR OF PUBLIC ACCOUNTS

Report on Compliance and on Internal Control Over Financial Reporting
Based on an Audit of the General-Purpose Financial Statements
Performed in Accordance With *Government Auditing Standards*

To the People of Kentucky
Honorable Paul E. Patton, Governor
Carol Palmore, Secretary, Personnel Cabinet

As part of the audit of the general-purpose financial statements of the Commonwealth of Kentucky as of and for the year ended June 30, 2001, we have audited payroll expenditures as recorded in the Management Administrative and Reporting System (MARS) for the general, special revenue, and internal service funds. We have also audited accrued leave obligations, accrued payroll expense, and applicable note disclosures of the Personnel Cabinet, an organizational unit of the Commonwealth as defined by KRS 12.010, and have issued our report thereon dated December 21, 2001. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Compliance

As part of obtaining reasonable assurance about whether the Commonwealth's financial statements are free of material misstatement, we performed tests of the Personnel Cabinet's compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Report on Compliance and on Internal Control Over Financial Reporting
Based on an Audit of the General-Purpose Financial Statements
Performed in Accordance with *Government Auditing Standards*
(Continued)

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Personnel Cabinet's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted a certain matter involving the internal control over financial reporting and its operation that we consider to be a reportable condition. A reportable condition involves matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the Personnel Cabinet's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable condition is described in the accompanying Schedule of Findings and Questioned Costs as item 01-PERS-1. In addition, we noted other matters involving internal control over financial reporting that are described in the accompanying schedule of findings and questioned costs of this report.

A material weakness is a condition in which the design or operation of one (1) or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, the reportable condition described in the schedule of findings and questioned costs is not a material weakness.

This report is intended solely for the information and use of management and applicable federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Respectfully submitted,



Edward B. Hatchett, Jr.
Auditor of Public Accounts

December 21, 2001

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

**PERSONNEL CABINET
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2001**

SECTION 1 - SUMMARY OF AUDITOR'S RESULTS

Financial Statement Accounts

Financial Statement Accounts: We issued an unqualified opinion on the Commonwealth's general-purpose financial statements, which included the Personnel Cabinet, as of and for the year ended June 30, 2001.

Internal Control Over Financial Reporting: Our consideration of the Personnel Cabinet's internal control over financial reporting disclosed one (1) reportable condition as described in Section 2 Financial Statement Findings. Our audit also disclosed other matters relating to the internal control over financial reporting for the Personnel Cabinet, which are also described herein.

Compliance: The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Federal Awards and Schedule of Expenditures of Federal Awards

This section is not applicable to the Personnel Cabinet.

Identification of Major Programs Audited

This section is not applicable to the Personnel Cabinet.

Dollar Threshold Used to Distinguish Between Type A and Type B Programs

The maximum dollar threshold used to distinguish between Type A and Type B Programs was \$15 million; however, there were no programs applicable to the Personnel Cabinet.

Auditee Risk

The Commonwealth did not qualify as a low-risk auditee.

**PERSONNEL CABINET
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2001
(CONTINUED)**

SECTION 2 - FINANCIAL STATEMENT FINDINGS

***Reportable Conditions Relating to Internal Controls and/or Reportable
Instances of Non-Compliance:***

**FINDING 01-PERS-1: The Personnel Cabinet Should Improve Security Controls For
Uniform Payroll And Personnel System Logical Access**

The Personnel Cabinet (Personnel) did not provide adequate logical security controls for access to the Uniform Payroll and Personnel System (UPPS). Despite our prior recommendations to limit access of GOT programmers to Personnel production load libraries, data files, and Job Control Language (JCL), our review specifically noted the following:

- Five (5) GOT programmers had update or control access via Time-Sharing Option (TSO) to production JCL and various datasets.
- One (1) of these GOT programmers also has update access to the Personnel Security files. This access gives them the ability to grant any users access to Personnel programs, JCL, or datasets. We understand Personnel uses the GOT programmer as a backup security administrator.

We also noted the Computer Security Policy/Procedure Manual (security policy) implemented by Personnel has not been updated since June 1997. As we had recommended in our prior audit, changes made to the Security List form during last year need to be reflected in the security policy, and thorough procedures for completing the form should be included. We had also recommended that instructions would be useful to explain the different levels of security access available and detail specific filing or retention policies of the Security List forms. Additionally, the current security policy does not include network intrusion detection proceedings.

Update access to the Personnel load libraries, production data, and security files should be restricted to Personnel staff only. Failure to maintain proper segregation of duties for GOT programmers increases the likelihood that an unauthorized change is possible to programs, JCL, or data. A strong control environment would not allow programmers access without adequate authorization and oversight. Circumstances of an emergency nature requiring update access privileges should be documented and closely monitored at the appropriate supervisory level. For those circumstances when it is necessary to grant update access to an application program, JCL, and/or dataset, a log should be created that specifically identifies the individual accessing the system by user ID, time of entry into the system, specific programs and data accessed, and purpose. All activity should be subject to supervisory control and system log entries should be substantiated by a formal request to make system changes or modify system access privileges.

**PERSONNEL CABINET
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2001
(CONTINUED)**

SECTION 2 - FINANCIAL STATEMENT FINDINGS

FINDING 01-PERS-1: The Personnel Cabinet Should Improve Security Controls For Uniform Payroll And Personnel System Logical Access (Continued)

Finally, formal security policies and procedures provide continuity for policy implementation, as well as set the tone of management concern for a strong system to secure assets and resources. These policies and procedures should be kept current, as they provide a security framework to educate management and users of their responsibilities.

Recommendation

We recommend Personnel take the following steps to improve logical security of UPPS:

- Eliminate all update and control accesses for GOT programmers. These employees should not have access to production data and/or JCL except in specific cases. Any update or control access granted to programmers should be documented and monitored closely by Personnel management. In addition, update access should be restricted to the level required to perform the assignment for a set time period and then rescinded. We recommend someone other than a GOT programmer be chosen as a backup security administrator.
- Update accordingly, and review periodically, the Personnel Cabinet Security Policy/Procedure Manual. The manual should include some general procedures concerning proceedings to identify and contend with unauthorized network intrusions.

Management Response and Corrective Action Plan

The Personnel Cabinet is currently mandated to maintain the official records of all state employees. It is further mandated to generate accurate and timely payroll tapes to ensure that all state employees are paid promptly on the 15th and 30th of each month.

The current statewide payroll/personnel system was implemented in 1982 and is an old mainframe COBOL system that has limited workflow. The system requires significant programming hours to ensure normal maintenance. All updates to the system have to be completed with the assistance of programmers from the Governor's Office of Technology, who have the sole expertise to make the necessary changes to the programs and/or data sets.

**PERSONNEL CABINET
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2001
(CONTINUED)**

SECTION 2 - FINANCIAL STATEMENT FINDINGS

FINDING 01-PERS-1: The Personnel Cabinet Should Improve Security Controls For Uniform Payroll And Personnel System Logical Access (Continued)

Management Response and Corrective Action Plan (Continued)

The Personnel Cabinet requires that all individuals having access to the system sign a security agreement before access is granted. This access creates an adequate audit trail of all users through the creation of a system log which specifically identifies the individual users by user ID, time of entry into the system and the specific program or data accessed during the entry to the system. This log is created and reviewed on a monthly basis.

As a result of the previous audit reports regarding adequate logical security controls, the Personnel Cabinet has recently established a Resource Management Analyst II position in the Department for Personnel Administration, Division of Employee Records, that will have primary responsibility for both internal and external access to the system. This position will work closely with agency liaisons and the Governor's Office of Technology staff in an effort to implement recommended security controls. This position will also be responsible for maintaining and updating the Computer Security Policy/Procedure Manual that was created in 1997.

The following specific exceptions to security controls are addressed as follows:

- *Five (5) GOT programmers had update or control access via Time Sharing Option (TSO) to production job control language and various datasets.*

The Personnel Cabinet has addressed this issue, in that access to those programmers has been rescinded until such time as they actually require access. Upon request for access, the security officer will grant that access on a time limited basis and again rescind access as appropriate.

- *One of these GOT programmers also has update access to the Personnel Security files.*

This update access has been eliminated. While this programmer will still need update capability at times, this is another area that the new security officer will control by granting and rescinding access on an as needed basis.

SECTION 3 - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

There were no federal award findings and questioned costs.

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

**PERSONNEL CABINET
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2001**

Fiscal Year	Finding Number	Findings	CFDA Number	Questioned Costs	Comments
<u>Reportable Conditions</u>					
<i>(1) Audit findings that have been fully corrected:</i>					
There were no findings for this section.					
<i>(2) Audit findings not corrected or partially corrected:</i>					
FY98	98-PERS-9	The Personnel Cabinet Should Implement Adequate Logical Access Security For The Unified Personnel And Payroll System	N/A	\$0	Although the agency took certain steps to control programmer access to production JCL and data, the steps taken were inadequate. However, they have now hired a full-time security employee to deal with this issue and intend to remedy the weakness.

(3) Corrective action taken is significantly different from corrective action previously reported:

There were no findings for this section.

(4) Audit finding is no longer valid or does not warrant further action:

There were no findings for this section.

Material Weaknesses

(1) Audit Findings that have been fully corrected:

There were no findings for this section.

(2) Audit findings not corrected or partially corrected:

There were no findings for this section.

(3) Corrective action taken is significantly different from corrective action previously reported:

There were no findings for this section.

(4) Audit finding is no longer valid or does not warrant further action:

There were no findings for this section.

**PERSONNEL CABINET
SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2001
(CONTINUED)**

Fiscal Year	Finding Number	Findings	CFDA Number	Questioned Costs	Comments
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Other Matters

(1) Audit findings that have been fully corrected:

FY 98	98-PERS-5	AOC Should Improve Controls Over Redeposits	N/A	\$0	Resolved during FY 01.
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(2) Audit findings not corrected or partially corrected:

FY 98	98-PERS-4	AOC Should Improve Controls Over Timesheets	N/A	\$0	An automated time sheet was developed and implemented for use by employees in the Frankfort Office July 1, 2002. The automated system will be implemented in Circuit Court Clerk's Office throughout the state January 2003.
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(3) Corrective action taken is significantly different from corrective action previously reported:

There were no findings for this section.

(4) Audit finding is no longer valid:

There were no findings for this section.

